February 3, 2005

Committee for Purchase From People
Who Are Blind or Severely Disabled
Attn. Docket No. 2004-01-01
1421 Jefferson Davis Highway
Jefferson Plaza 2, Suite 10800
Arlington, Virginia 22202-3259

Re: Comments submitted by a JWOD producer **Docket No. 2002-01-01,** "Governance Standards for Central Nonprofit Agencies and Nonprofit Agencies Participating in the Javits-Wagner-O'Day Program"

To Whom it May Concern:

Our organization is a successful JWOD contractor, and has been for many years. We employ several hundred people who have severe to profound disabilities in our JWOD operations. None of these people would have any employment were it not for the JWOD program. They are simply not employable in competitive employment settings. We have grave concerns over the Committee's proposed publication of new and legislatively unsupported rules for organizations such as ours. And because of the climate and tone of these proposed rules, we fear that even to identify our organization will cause irreparable harm to us and our employees. As capricious as these rules seem, it is not a stretch to envision a Committee bent on retaliating against organizations that do not toe the line. Hence, our anonymity.

If passed, the "Governance Standards for Central Nonprofit Agencies and Nonprofit Agencies Participating in the Javits-Wagner-O'Day Program" that has been proposed by the Committee for Purchase from People Who Are Blind or Severely Disabled ("the Committee"), 69 Federal. Reg. 218, 65395 *et seq.*, will directly and adversely affect the ability of our agency and all similar organizations to provide continued employment to persons with disabilities. Accordingly, we submit this comment and urge the Committee to abandon its proposed rule on the grounds that it: (i) exceeds the Committee's rulemaking authority and is not supported by the JWOD Act's legislative history; (ii) is arbitrary and capricious; (iii) violates Equal Protection principles and engenders discriminatory application; (iv) is duplicative of the Internal Revenue Code and other regulatory systems; (v) weakens agency boards and creates agency instability; and (vi) endangers the continued success of the JWOD Program.

I. The Proposed Rule Exceeds the Committee's Rulemaking Authority and Is Not Supported by the JWOD Act's Legislative History

In 1938, Congress granted the Committee authority to "make such rules and regulations regarding specifications, time of delivery, authorization of a central nonprofit making agency to facilitate the distribution of orders among the agencies for the blind, and other **relevant matters of procedure** as shall be necessary to carry out the purposes of the JWOD Act."[1] When it amended the Act in 1971, Congress preserved this restrictive mandate, granting the Committee the limited power to: (i) establish procurement lists for the commodities and services that the government will purchase from JWOD-affiliated agencies; (ii) set the market price for those goods and services; and (iii) make rules and regulations regarding the specifications for commodities and services on the procurement list, the time of their delivery, and "such other matters as may be **necessary** to carry out the purposes of" the JWOD Act.[2] The Committee cannot promulgate any rules that do not fall within this statutorily granted authority.[3] Further, the Act clearly defines a "**qualified** nonprofit agency" that is permitted to participate in these procurement activities. (41 U.S.C § 48b) Therefore, to introduce new qualifying standards that are not contained in the Act, would require no less than Congressional action.

However, the Committee now proposes to grant itself the authority to re-define qualified nonprofit agencies, to dictate how JWOD-affiliated agencies will be governed, and to review agency executive compensation to determine whether it is "reasonable."[4] This proposal, in it's entirety, clearly exceeds the Committee's statutory authority to re-define qualified nonprofit agencies and to make rules and regulations that go beyond the procurement of goods and services from agencies that employ the blind and severely disabled, and there is nothing in the JWOD Act's legislative history that would warrant a broader interpretation of these limited powers.

To the extent that the Committee seeks to invoke its power to make such rules as are necessary to carry out the purposes of the JWOD Act, those powers are statutorily tied to the Committee's authority to establish procurement-related regulations and rules. Further, as the Committee recognizes, Congress's purpose in establishing the JWOD Program was to

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[1] 41 U.S.C. § 47, amendments (emphasis added).

[2] 41 U.S.C. § 47 (emphasis added).

[3] 5 U.S.C. § 706; *Killip v. Office of Pers. Mgmt.*, 991 F.2d 1564, 1569 (Fed. Cir. 1993) ("Though an agency may promulgate rules or regulations pursuant to authority granted by Congress, no such rule or regulation can confer on the agency any greater authority than that conferred under the governing statute.").

[4] 69 Fed. Reg. 218, 65397.

provide Americans who are blind or who have severe disabilities "with meaningful employment opportunities while providing the Federal Government with quality products and services, delivered on time and at a fair market price."[5] The Committee has not demonstrated how its proposed regulations are **necessary** to increase employment opportunities for the blind and severely disabled or to increase the quality, price, and timely delivery of goods and services to the federal government. Accordingly, the Committee's unprecedented proposal clearly exceeds the Committee's Congressional mandate and, if passed, will not withstand judicial review.[6]

II. The Proposed Rule Is Arbitrary and Capricious

In addition to exceeding the Committee's rulemaking authority, the Committee's proposed rule is irrational, rendering it both arbitrary and capricious.[7] Specifically, the proposed rule is: (i) based upon unsubstantiated rumor that the Committee concedes is largely inapplicable to JWOD-affiliated agencies; (ii) premised upon irrational compensation standards; and (iii) irrationally based upon the receipt of federal funds. Accordingly, the proposed rule is not only ill conceived, but legally unsupportable.

A. The Need for the Proposed Rule is Unsubstantiated

The Committee declares that the proposed governance rules are being promulgated in response to "recent accounts *alleging*, and public concern regarding, *isolated* instances of excessive compensation packages for nonprofit agency executives; a *perceived* lack of full disclosure in the financial reporting of nonprofit agencies; and the absence of formal guidelines to establish independent boards of directors for JWOD-affiliated . . . agencies."[8] Thus, the Committee's proposal is based upon little more than speculation and rumor regarding *isolated* instances of excessive compensation for nonprofit agencies. The Committee has **not** determined whether this public concern can be substantiated or whether

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[5] COMMITTEE FOR PURCHASE FROM PEOPLE WHO ARE BLIND OR SEVERELY DISABLED, *2003 Annual Report*, Chairman's Message.

[6] *See, e.g., Bowen v. Georgetown Univ. Hosp.*, 488 U.S. 204, 208 (1988) ("It is axiomatic that an administrative agency's power to promulgate legislative regulations is limited to the authority delegated by Congress."); *Nat'l Retired Teachers Ass'n v. U.S. Postal Serv.*, 430 F. Supp. 141, 145 (D.D.C. 1977) ("It is well-settled that a regulation which exceeds Congressional authorization is invalid.").

[7] 5 U.S.C. § 706; *Motor Vehicle Mfr. Assoc. v. State Farm Mut. Ins. Co.*, 463 U.S. 29, 42-43 (1983) (holding that irrational rules are arbitrary and capricious and, therefore, invalid).

[8] 69 Fed. Reg. 218, 65395-65396 (emphasis added).

it is associated with JWOD-affiliated agencies. In fact, the Committee concedes that it "believes, based on its experience managing the JWOD Program, that the **overwhelming majority** of JWOD-affiliated . . . agencies operate in an ethical and accountable manner."[9] Accordingly, the Committee's proposed rule is a knee jerk reaction to unsubstantiated factors and a few alleged acts of corporate abuse.

B. The Proposal Contains Irrational Compensation Standards

The Committee lists seven factors that it will consider when determining whether agency executive compensation is "reasonable:" (i) the size and complexity of the agency's mission; (ii) the agency's mission area, geographic size, and financial condition; (iii) the qualifications and experience required of executives; (iv) compensation packages at comparable agencies; (v) the percentage of JWOD-generated revenue paid to executives; (vi) the extent to which executive compensation packages exceed that which is paid to the typical, highest paid SES career federal employee; and (vii) a comparison of executive versus labor force compensation.[10] However, the Committee explains in the preamble that it will "generally consider" any compensation package that exceeds the compensation package offered to the typical, highest paid SES career federal government employee (or approximately $207,000) unreasonable.

The Committee has neither the time nor expertise needed to fully and fairly evaluate each agency's complexity, mission, financial condition, and leadership qualifications. Moreover, the comparison of agencies to determine whether compensation among them is comparable requires sophisticated analysis that, if done incorrectly or inconsistently, may lead to discriminatory application. To the extent that the Committee intends for the agencies to conduct that analysis themselves, such a requirement would place an undue burden on many agencies that, because of their nonprofit status, operate on a restricted budget. Further, the percentage of revenue that JWOD-affiliated agencies pay their executives, as well as the difference between executive compensation and labor force compensation, are unworkable standards that do not account for the duties and responsibilities borne by agency executives or the fact that JWOD-affiliated agencies employ individuals who are not otherwise competitive in the labor market.

More importantly, the Committee provides no rational explanation for its decision to tie agency executive compensation to the compensation earned by federal employees. Unlike agency executives, federal employees enjoy unique job security; guaranteed post-retirement and early retirement benefits; bonuses, promotions, and retention allowances; and shared responsibility for individualized units instead of unmitigated responsibility for an entire

[9] *Id.* at 65396 (emphasis added).

[10] *Id.* at 65400.

enterprise. Moreover, the compensation that nonprofit agencies offer their executives depends largely upon market forces such as: the compensation packages that are offered to similarly situated professionals in the for-profit sector; the level of responsibility and risk that each executive is expected to bear; and the success that each executive brings to the organization. Many of these individuals operate multi-million dollar agencies that, with the exception of their nonprofit status, are no different than multi-million dollar private companies, whose executives earn substantially higher salaries. In fact, the nonprofit and heavily regulated status of JWOD-affiliated agencies, as well as the difficulties that are inherent in running an agency whose primary workforce is blind or severely disabled, requires even greater skill and expertise than that which is required of many for-profit executives.

Finally, Chief Executive Officers and other agency leaders are directly, and sometimes personally, responsible for their agencies' success. It is not uncommon for agency leaders to personally guarantee credit lines or bank notes to ensure the agency's continued operations. Thus, agency executives shoulder significant personal risks and responsibilities that federal employees simply do not experience. Their compensation should reflect that risk and responsibility.

C. Regulation Due to the Receipt of Federal Funds is Irrational

Finally, the Committee explains that "[t]he basis for comparing a . . . nonprofit agency's executive compensation to a Federal employee's compensation lies in the fact that the JWOD Program is a Federal program and the funds obtained through the JWOD Program are Federal contract funds."[11] The comparison of federal and private executive compensation because of the receipt of federal funds is entirely irrational. Under the JWOD Program, government funds are used to *purchase* goods and services; they are not used to fund the agencies themselves. These are not Grant funds. Thus, the Committee is only able to limit government expenditures by establishing procurement lists and setting market prices for the goods and services that it will purchase through the JWOD program.

Moreover, as discussed below, JWOD-affiliated agencies are no different than the countless for-profit entities that receive federal dollars in exchange for goods and services. Accordingly, the selection of JWOD-affiliated agencies for this unique form of government oversight is arbitrary, capricious, and indefensible.

[11] *Id.* at 65395, 65397.

III. The Proposed Rule Violates Equal Protection Principles and Engenders Discriminatory Application

The Committee's proposed rule is not only arbitrary and capricious; it violates Equal Protection principles. Federal funds are used to purchase goods and services from numerous for-profit private companies, including, for example, Halliburton, Raytheon, General Electric, AT&T, Bechtel, Boeing, and Lockheed Martin. The vast majority of our organizations, while nonprofit, are privately operated and not limited to conducting business with the federal government. In fact, many of the larger JWOD-affiliated agencies derive only a small percentage of their income through the JWOD Program. Thus, with the exception of their nonprofit status, they are no different than General Electric and countless other companies that receive federal contract funds. Accordingly, the Committee's proposal to single out JWOD-affiliated agencies for this disparate treatment is patently discriminatory.

In addition to this blatant discrimination, the proposed rule contains undefined terms and standards that may result in discriminatory application. For example, the Committee lists seven factors that it will consider when determining whether executive compensation is reasonable. The Committee does not indicate how these items will be weighed or whether standards will be established to ensure uniform application. Moreover, the Committee indicates that it "would generally consider" an agency's executive compensation package unreasonable if it exceeds the total compensation package offered the typical, highest paid career federal employee, "unless the . . . agency can provide adequate justification for the level of executive compensation to the Committee." The Committee does not define what will constitute "adequate justification" for those compensation packages that exceed the approximately $207,000 cap. Presumably, therefore, that determination is left to the Committee's unfettered discretion. This unfettered discretion paves the way for discriminatory treatment, whether actual or perceived.

IV. The Proposed Rule Is Duplicative of the Internal Revenue Code and Other Regulatory Systems

The Committee admits that "the information that . . . agencies would provide to us would be the same as what is required under Part IV of the IRS From 990," according to which agencies must disclose their administrative expenses and executive compensation.[12] Moreover, Internal Revenue Code ("IRC") §§ 501(c)(3) and 4958 already prohibit JWOD-affiliated agencies from paying their executives unreasonable compensation, the penalties for which include loss of exempt status and significant monetary penalties for both the executives who receive unreasonable compensation and the individuals who approve such

[12] *Id.* at 65398

compensation packages.[13] Accordingly, the Internal Revenue Service ("IRS") fully regulates the compensation that may be paid to executives of nonprofit agencies, and the Committee's proposed rule is duplicative.

Moreover, there is no suggestion that the IRC and corresponding regulations are ineffectual. In fact, in July 2004, the IRS commenced a new enforcement effort to identify and halt abuses by tax-exempt organizations that pay excessive compensation and benefits to their officers and other insiders.[14] Under that effort, which will continue into 2005, the IRS is in the process of examining nearly 2,000 agencies to determine whether nonprofit executive compensation is reasonable.[15] If the Committee is concerned about the fiscal management of a few, isolated agencies, it may simply report those entities to the IRS. Thus, in addition to duplicating the IRC, the Committee's proposed rule is entirely unnecessary.

Further, the Committee's proposed definition of what constitutes "reasonable" executive compensation conflicts with the IRC and its corresponding regulations. Under the IRC, reasonable compensation is defined as the amount that would ordinarily be paid for "like services" by "like organizations" in "like circumstances."[16] As discussed above, federal employees and agency executives do not perform "like services" in "like organizations" under "like circumstances." Moreover, whether executive compensation is reasonable under the IRC is a question of fact that must be determined by reviewing all of the applicable circumstances.[17] The Committee's proposal that any compensation in excess of approximately $207,000 will be presumptively unreasonable constitutes a predetermination of what is reasonable and, therefore, is without consideration of the underlying facts or circumstances. Accordingly, the Committee's proposed rule is inconsistent with the IRC.

Finally, numerous other regulatory systems govern nonprofit agencies to ensure that the citizens they are commissioned with promoting—in this case, the blind and disabled—are adequately protected from corporate abuse. Congress itself, through the Senate Finance Committee, scrutinizes nonprofit governance standards. Moreover, nonprofit agencies are organized under state law, which imposes restrictions on the governance of nonprofit agencies, charitable trusts, and charitable activities. These restrictions are enforced by state

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[13] 41 U.S.C. § 48b(4)(a); 26 U.S.C. §§ 501(c)(3), 503(b), 4958; 26 C.F.R. 1.501(c)(3)-1(c)(2); *Mabee Petroleum Corp. v. U.S.*, 203 F.2d 872, 876 (5th Cir. 1953) (excessive salaries create inurement).

[14] INTERNAL REVENUE SERVICE, *IRS Initiative Will Scrutinize EO Compensation Practices*, August 10, 2004, available at IRS.gov.

[15] *Id.*

[16] 26 C.F.R. 1.162-7(b)(3).

[17] *Mabee*, 203 F.2d at 875.

Attorneys General, whose concentrated areas of responsibility make them far more capable of enforcing governance standards than the Committee, which proposes to annually police countless nonprofit agencies that are distributed throughout the United States. Accordingly, the Committee's proposed rule unnecessarily duplicates other nonprofit regulatory schemes, thereby placing a tremendous burden on JWOD-affiliated agencies for no perceptible gain.

V. The Proposed Rule Weakens Agency Boards and Creates Agency Instability

In addition to mandating what will constitute reasonable compensation for agency executives, the Committee's proposed rule requires agencies to: (i) "turn over" their Board "on a recurring schedule;" and (ii) publish and make public the "minutes of Board, or other governing authority, meetings."[18] These proposals do little more than create a facade of proper governance while placing unjustifiable restrictions on agency Boards of Directors ("Boards") that serve only to weaken those Boards and create agency instability.

Smaller agencies are not always able to find qualified or willing candidates to assume Board positions, particularly when those positions must be filled on a volunteer basis. Thus, by requiring Boards to place arbitrary term limits on their members, the Committee creates a danger that agencies will have to accept less qualified or less committed Board members for the sole purpose of complying with the Committee's regulations. Moreover, there are circumstances when Board continuity and sustained institutional knowledge are needed to ensure agency stability and growth. Each Board—not the Committee—is equipped with the knowledge and experience needed to make this determination, the limitations for which are firmly rooted in each Board's fiduciary obligation to its agency. Finally, agencies that depend upon financial institutions for lines of credit or other loans may be required to give lending institutions a position on the Board. By requiring agencies to turn over their Boards on an undefined "recurring schedule," the Committee may unwittingly render some agencies unable to obtain the financial support they need to participate in the JWOD Program.

The Committee's proposal regarding the publication of Board meetings is equally problematic. First, it substantially chills the ability of Boards to fully discuss competitive, development, and personnel issues without fear of public disclosure or potential liability. Many JWOD-participating agencies compete with other nonprofit agencies and for-profit companies that do not participate in the JWOD Program. These competitors may use the published minutes to gain an unfair advantage by determining, for example, the direction of agency growth and development, thereby substantially weakening the agencies' market position. In addition, many JWOD-affiliated agencies operate on a limited budget. Publishing the minutes of their board meetings—in addition to complying with all of the other reporting requirements contained within the proposed rule—will entail substantial

[18] 69 Fed. Reg. 218, 65400.

expense and administrative burden, further weakening the agencies' ability to focus their resources on employment of the blind and severely disabled.

VI. The Proposed Rule Endangers the Future Success of the JWOD Program

The JWOD Program is, by all accounts, achieving its goals at a rapid rate, as demonstrated by the fact that, in 2003, there was an 11% increase in total direct labor hours worked by individuals who are blind or severely disabled, and a 16% increase in those individuals' salaries.[19] This success can be attributed in large part to the fact that, under the JWOD Program, participating agencies enjoy both corporate autonomy and a reliable customer base that will purchase goods and services at a pre-determined price. However, if the Committee succeeds in nationalizing the fiscal management and governance of JWOD-affiliated agencies, this autonomy will no longer exist, thereby removing one of the primary incentives to private enterprise. Further, the uncertainty that is inherent in the Committee's discretion to annually determine which executive compensation packages are reasonable; whether Board turn over is adequate; or whether each agency has otherwise complied with the remaining, largely undefined, provisions of the proposed rule destroys the stability that the JWOD Program formerly provided to affiliated agencies. Accordingly, individuals and entities will be less inclined to participate in the JWOD Program. Ours certainly would be.

Further, most of the growth in JWOD-affiliated agencies in recent years has been by privately operated entities, the success of which depends on their ability to recruit and retain quality professionals, whose leadership will foster agency growth and, consequently, competitive employment opportunities for the blind and severely disabled. The Committee's proposed rule limits agencies' ability to establish executive compensation schemes that account for the quality of leadership each agency requires and that compensate its executives according to the amount paid for "like services" by "like organizations" in "like circumstances." Thus, there is a grave danger that JWOD-qualifying agencies will lose quality leaders and either cease to exist or cease to grow. Accordingly, the Committee's proposed rule is highly detrimental to the future establishment of qualifying agencies and the continued success of existing agencies, thereby endangering the extent to which employment opportunities to the blind and severely disabled will be available in the future.

Finally, if passed, the proposed rule will disqualify many agencies that currently participate in the JWOD Program. This disqualification will lead to the loss of countless jobs for the blind and severely disabled, thereby ending 30 years of meaningful and remunerative employment for people who, without JWOD, have little or no hope of employment. It is inconceivable that Congress intended for the Committee to *reduce* job opportunities for the

[19] JWOD 2003 Annual Report.

blind and disabled for the dubious public relations benefit of claiming that none of the agencies who participate in the Program pay their executives more than $207,000.

VII. Conclusion

As this comment illustrates, the Committee's proposed rule: (i) exceeds the Committee's rulemaking authority and is not supported by the JWOD Act's legislative history; (ii) is arbitrary and capricious; (iii) violates Equal Protection principles and engenders discriminatory application; (iv) is duplicative of the Internal Revenue Code and other regulatory systems; (v) weakens agency boards and creates agency instability; and (vi) endangers the continued success of the JWOD Program. If passed, it will have dire consequences on the ability of countless, heretofore qualified, nonprofit agencies to provide continued employment opportunities to the blind and severely disabled. Accordingly, we strongly urge the Committee to cease its efforts to regulate the governance and fiscal management of JWOD-affiliated agencies and leave these tasks to the laws and agencies already established by Congress for that purpose. The time, effort and resources required to support this proposed action would be much better spent working to support the JWOD mission of increasing employment opportunities for individuals who are blind or severely disabled...the Committee's Congressionally mandated mission.

Thank you for the opportunity to submit this comment.

Respectfully Submitted;

The Board of Directors
Of a Qualified Nonprofit Agency
As Defined at 41 U.S.C § 48b

PS: It would be fair for the Committee to wonder – what is it that we have to hide. The answer? Nothing. Our agency would largely be in compliance today. But we do not now, nor will we ever publish the minutes of our Board meetings. The United States Government is not our only customer and other nonprofits are not our only competitors. If we were required to do so, we would either drop out of JWOD, or seek judicial protection for our investments and our employees.